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No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

PHILKO AVIATION, INC.,

Petitioner,

vs.

MAURICE SHACKET and SYLVIA SHACKET,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED

A. By enacting Section 1403 of the Federal Aviation Act, 49 U.S.C. Section 1403 (1981), requiring the recordation of conveyances affecting aircraft, did Congress preempt state law insofar as state law would permit the conveyance of title to aircraft by transfer of possession alone, without FAA recording?

B. May a federal claim for civil damages be maintained under Section 1403 of the Federal Aviation Act, 49 U.S.C. Section 1403 (1981), by an aircraft purchaser or financer against a prior unrecorded purchaser of the same aircraft, where the first purchaser has ignored the FAA recording requirements and the subsequent purchaser or financer relies to his detriment on the status of title shown in the FAA registry and buys or extends credit on the strength of such title?

C. Should Plaintiff Shacket be estopped from asserting title to the aircraft at issue because he failed to record his purported conveyance with the FAA?

Philko Aviation, Inc., the Petitioner herein, is a wholly owned subsidiary of McArdle, Ltd., a Delaware Corporation. Philko Aviation, Inc. has no subsidiaries. McArdle, Ltd. has the following wholly owned subsidiaries in addition to Philko Aviation, Inc.: Airport Farms, Inc.; American Lodging Corp.; Big Flamingo II, Inc.; Bonhomme Richard, Ltd.; Burr Hill Country Club Inc.; Burr Hill Properties, Ltd.; Forty-Six East Oak, Ltd.; Pheasant Run, Inc.; Rockton Productions, Inc.; Smith Road Properties, Ltd.; Spanish Lakes, Inc. and Wilson World Travel, Inc.

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In The

Supreme Court of the United States

October Term, 1982

PHILKO AVIATION, INC.,

Petitioner,

vs.

MAURICE SHACKET and SYLVIA SHACKET,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

The petitioner Philko Aviation, Inc. respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit entered in this proceeding on June 22, 1982.

OPINIONS BELOW

The opinion of the Court of Appeals, not yet reported, appears in the Appendix A hereto. The opinion of the District Court for the Northern District of Illinois is published at 497 F. Supp. 1262 (N.D. Ill. 1980). A copy of the district court's declaratory judgment order and two memorandum opinions are attached as Appendix B, C and D.

JURISDICTION

The judgment of the Court of Appeals for the Seventh Circuit was entered on June 22, 1982 and this petition for certiorari was filed within sixty days of that date. This Court's jurisdiction is invoked under 28 U.S.C. Sec. 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Article VI of the United States Constitution

49 U.S.C. Sec. 1403 (1964)

49 U.S.C. Sec. 1406 (1964)

Uniform Commercial Code Section 2-403, Ill. Rev. Stat. Ch. 26 Sec. 2-403 (1980).

The full text of these constitutional and statutory provisions are included in Appendix F.

STATEMENT OF THE CASE

On April 19, 1978 pursuant to a contract of sale, Maurice and Sylvia Shacket attempted to purchase a 1978 Piper Navajo, Serial Number 78MS, from Roger Smith Aircraft Sales Inc. (Smith Inc.) in Aurora, Illinois. The purchase price was to be $126,000 plus the trade-in of

Mr. Shacket's existing aircraft. Shacket met Roger Smith, President of Smith Inc., in Aurora on April 19, 1978 and paid Smith Inc. $106,000. Prior to this date, Shacket had paid $20,000 and had delivered his trade-in aircraft to Smith, Inc. Although Maurice Shacket, an experienced pilot, was familiar with FAA recording requirements and had himself prepared a bill of sale and a registration form at a previous aircraft purchase, he did not obtain the original bills of sale for the 78MS aircraft from Smith Inc. Moreover, Shacket retained the bills of sale on his trade-in aircraft pending receipt of the original bills of sale from Smith Inc. On April 19, 1978 Shacket took possession of the aircraft and flew it to the State of Michigan where he resides.

On April 21, 1978 Smith Inc. offered to sell the same Piper Navajo 78MS to Philko Aviation Inc. (Philko). Smith Inc. demonstrated a clear chain of title by presenting to Philko the original bills of sale from the manufacturer, Piper, through two intervening dealers, North States Aviation and Clark Aviation, to Smith Inc. (See Appendix E).

Smith Inc. offered to sell the aircraft to Philko for $212,000. At that time Smith Inc. was obligated to Philko for $60,000. This debt had arisen out of a loan by Philko to Smith Inc. The purchase price of $212,000 was to be paid by Philko in the form of $152,000 in cash and the cancellation of the $60,000 debt. Roger Smith persuaded Philko to enter into this transaction by falsely representing *inter alia* that Smith Inc. had a ready buyer for the plane, named Krueger Aviation, to whom Philko could sell the plane if it so desired. Philko obtained a loan of $152,000 from the Sandwich State Bank in Sandwich, Illinois. Philko, through an agent of the Sandwich State Bank, verified the status of the title with the FAA in Oklahoma City. The FAA register showed that Piper Aircraft Corporation had manufactured

this new aircraft and that record notification had been submitted by Piper showing a proposed transfer to North States Aviation, an authorized Piper distributor. (Deposition of Richard Andrews, Vice President of Sandwich State Bank, pp. 81-86.) Philko paid $152,000 to Smith Inc. and cancelled the existing debt. Philko then recorded the original bills of sale and the Sandwich State Bank recorded its chattel mortgage on the aircraft for $152,000.

Shacket then filed a two count suit. The first count sought a declaratory judgment pursuant to 29 U.S.C. Sec. 2255 (1981) that title to the aircraft rested in Shacket. The second count alleged fraud against Philko and Smith Inc. Philko filed a counterclaim in two counts, seeking a declaratory judgment of title in Philko and the second seeking damages of $160,000. Philko also raised by way of affirmative defense a claim of estoppel based on Shacket's failure to record.

Although Shacket's complaint alleged federal jurisdiction on the basis of diversity pursuant to 28 U.S.C. Sec. 1332 (1981), neither the district court nor the Court of Appeals below articulated the jurisdictional basis upon which the judgment order was entered. Philko submits that the District Court had original jurisdiction pursuant to 29 U.S.C. Sec. 1331 because this case presents federal questions arising under Section 1403 of the Federal Aviation Act and the Supremacy Clause, Article VI of the United States Constitution.

Both parties filed cross motions for summary judgment. Shacket sought a declaration of title in him and damages for fraud. Philko sought a declaration of title in its favor and damages of $160,000 on its counterclaim. The district court entered a judgment declaring title to the aircraft in Shacket and denying all other relief requested by the parties.

REASONS FOR GRANTING THE WRIT

1.

THE DECISION BELOW CONFLICTS IN PRINCIPLE WITH THE DECISIONS OF OTHER COURTS OF APPEAL, AND CONFLICTS WITH DECISIONS OF THE SUPREME COURT OF THE STATES OF CALIFORNIA AND OKLAHOMA CONCERNING THE PREEMPTIVE EFFECT OF SECTION 1403.

The present controversy is engendered by a conflict between Section 1403(c) of the Federal Aviation Act, 49 U.S.C. Sec. 1403 (1981), and Section 2-403 of the Uniform Commercial Code which has been adopted by virtually every state. Section 1403(c) invalidates unrecorded conveyances of title to aircraft as against third parties without notice. Section 2-403 of the Uniform Commercial Code authorizes the valid conveyance of title to goods, including aircraft, merely by the transfer of possession. Under the Supremacy Clause, the federal recording requirement must be given precedence. Otherwise the legitimate Congressional objective of providing a reliable central register for instruments affecting aircraft title will be frustrated.

The decision of the Court below judicially repeals Section 1403(c). Under its holding Shacket failed to record, Philko relied upon the status of title shown at the FAA register and duly recorded his conveyance, but Shacket nevertheless prevailed. This decision conflicts in principle with the opinions of the Third, Fourth, Fifth, Ninth and Tenth Circuits. Although the Courts of these Circuits have recognized, specifically in light of Section 1406, 49 U.S.C. Sec. 1406 (1981), that 1403 has a limited preemptive effect, they nevertheless agree that in enacting Section 1403 Congress intended a mandatory central filing register. Congress' avowed purpose was to provide

aircraft purchasers and encumbrancers with a single, central location to which they could look for instruments affecting title to aircraft. This Congressional purpose was evident in the original Civil Aeronautics Act of 1938. Section 523 of the Civil Aeronautics Act was reenacted substantially unchanged as Section 1403 of the Federal Aviation Act of 1958. 2 U.S. Code Cong. & Ad. News 3755 (1958). Congress left Section 1403 intact when it enacted Section 1406 in 1964. In enacting Section 1406, Congress federalized the choice of law rules for testing the substantive validity of such instruments, but it did not modify or eliminate the recording requirement.

The Third Circuit in *Sanders v. M. D. Aircraft Sales, Inc.*, 575 F.2d 1086 (3rd Cir. 1978) decided that the Federal Aviation Act did not preempt state law insofar as the substantive validity of a *recorded* security interest in an aircraft was concerned. This case presented a dispute between a floor plan financing company and a buyer in the ordinary course of business and is typical of many of the reported decisions. In ruling in favor of the buyer, the Court looked to underlying state law (Section 9-307 of the Uniform Commercial Code) to test the substantive validity of a recorded security interest. The Court, however, recognized that through Section 1403 Congress had adopted a federal recording system. *Id.* at 1088.

The Fourth Circuit in *Haynes v. General Elec. Credit Corp.*, 582 F.2d 869 (4th Cir. 1978) affirmed *per curiam* a decision of the District Court for the Western District of Virginia in favor of a buyer in the ordinary course over a prior recorded secured lender. Both parties had recorded in conformance with FAA requirements. The District Court in that case had expressly stated that "federal law governs the relative rights of third parties

and other claimants to the aircraft only to the extent that those rights are dependent on the *fact* or time of recordation." *Id.* at 767. (Emphasis added.) The case now before this Court should be determined by federal law because Shacket's rights in the aircraft are initially dependent on his recording. Until Shacket recorded an instrument, as to third parties his purported conveyance was invalid.

The Fifth Circuit in *Bank of Lexington v. Jack Adams Aircraft Sales, Inc.*, 570 F.2d 1220 (5th Cir. 1978) was faced with a dispute between two recorded security interests. The Court expressly recognized that the Federal Aviation Act created a framework for a nationwide system to record certain interests in aircraft. To the extent that state law conflicts with any part of the Act, the Court held that state law was preempted. *Id.* at 1224.

The Ninth Circuit Court of Appeals in *CIM International v. United States*, 641 F.2d 671 (9th Cir. 1980) noted that the purpose of the recording provisions of Section 1403 is to protect persons who have dealt on the faith of the FAA register so as to lend stability in a nationwide market for aircraft, a highly mobile product. *Id.* at 674. The Court further stated that it is wrong "to favor a party who totally ignored the FAA registry to the detriment of the party who apparently respected it." *Id.* at 676. *CIM International, id.*, presented a dispute between the assignee of a recorded aircraft security interest against an unrecorded federal tax lien. Because CIM purchased the secured creditor's interest in the aircraft on the strength of the title as shown in the FAA register, it prevailed over the unrecorded tax liens which arose prior to CIM's purchase.

The Tenth Circuit in *State Securities Co. v. Aviation Enterprise*, 355 F.2d 225 (10th Cir. 1966), ruled in favor

of a buyer in the ordinary course of business as against an unrecorded secured lender who claimed a chattel mortgage on an aircraft. Neither party had recorded with the FAA, but the buyer attempted to record his bill of sale. The Tenth Circuit unequivocally recognized that "[B]y providing a federal system for registration of conveyances and liens affecting title to aircraft, Congress has preempted that field and state recording statutes are not applicable to such title instruments." *Id.* at 229. If a state statute which would mandate recording aircraft title interests in a place other than the FAA register is preempted by Section 1403, it follows that a state statute (namely 2-403) which would entirely dispense with recording the conveyance of title to aircraft is also preempted and should be given no effect.

Two state Supreme Courts have recognized the preemptive effect of Section 1403: *Dowell v. Beech Acceptance Corporation*, 91 Cal. Rptr. 1, 476 P.2d 401 (1971), and *McCormack v. Air Center Inc.*, 571 P.2d 835 (Supreme Court of Oklahoma, 1977). The former held that the federal recording requirement absolutely preempted state law, even to the point that a buyer in the ordinary course does not find protection against a prior secured lender under Section 9-307 of the UCC. The latter held that the federal recording statute supplanted the Oklahoma artisan's lien statute insofar as the state statute mandated recording a lien in a place other than the FAA register.

The decision below is also at odds with the decisions of many lower courts which have held that the party who relies upon the FAA title register should prevail over one who has failed to record. For example, in *Marsden v. Southern Flight Service Inc.*, 227 F. Supp. 411 (M.D. N.C. 1961), a lender who extended credit on the strength of title shown in the FAA register was given

priority over a prior purchaser who failed to record his conveyance. In *Blalock v. Brown*, 78 Ga. App. 537, 51 S.E.2d 610 (1949) the Georgia appellate court held that as between two purchasers of the same aircraft, the second purchaser should prevail where the first purchaser failed to record his conveyance with the FAA. See also *O'Neill v. Barnett Bank of Jacksonville, N.A.*, 360 So. 2d 150 (1978). Petitioner Philko submits that if this case had been filed in California, Oklahoma, Florida or North Carolina, the opposite result would have been obtained. The state courts of other states will undoubtedly be faced with the task of determining the preemptive effect of Section 1403 in the future. A pronouncement by this Court as to the preemptive effect of Section 1403 will give this unsettled area of the law urgently needed uniformity.

It is clear from many decided cases that a purchaser or lien creditor cannot have a valid interest as against any third party without notice unless he records. In a dispute between or among holders of competing *recorded instruments*, substantive state law should determine the outcome as Section 1406 plainly states. The decisions of the District Court and the Court of Appeals below, however, go beyond this plain intent and meaning of Sections 1403 and 1406. By giving Shacket's unrecorded interest priority over that of Philko, they have created an exception to the recording requirement which swallows the rule. Because of the decision below, it is now imprudent, if not impossible, to rely upon the status of title shown at the FAA register. A buyer such as Philko, even if he takes possession, cannot determine whether the aircraft he is purchasing was the subject of a prior purchase. The decision below casts aircraft title and financing law back to the chaotic posture it was in before the Civil Aeronautics Act was enacted. If title to an aircraft can be conveyed without the delivery of any

written instrument, as in Shacket's case, the choice of law rules of Section 1406 are also rendered inoperable. The decision below has clearly misconstrued Section 1403 and Petitioner requests the Court to grant a writ of certiorari to review this decision.

2.

THE ISSUE OF THE EXTENT TO WHICH SECTION 1403 OF THE FEDERAL AVIATION ACT PREEMPTS STATE LAW IS ONE OF MAJOR IMPORTANCE TO THE INCREASING NUMBER OF PERSONS DEALING IN THE PURCHASE, USE AND FINANCING OF AIRCRAFT, ONE OF THE MOST HIGHLY MOBILE OBJECTS IN INTERSTATE COMMERCE.

Both federal and state courts are faced with the task of construing Section 1403 in disputes concerning title to aircraft. Because of the ever increasing volume of aircraft sales and financing, the prevalence of such disputes can be expected to continue and grow. Several commentators have expressed that a decision on the preemption issue by the Supreme Court, the final arbiter of questions of federal law, would go far to remove significant uncertainties and conflicts in connection with priorities among competing interests in aircraft and the relationship of the FAA act to state law.[1] The present controversy squarely poses the preemption question. It presents an opportunity for this Court to reduce litigation in this area by eliminating a piecemeal and inconsistent evolution of principles regarding the preemptive effect of Section 1403 and the relationship of FAA recording to state law.

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[1] *See e.g.*, Sigman, The Wild Blue Yonder: Interests in Aircraft Under Our Federal System, 46 So. Cal. L. Rev. 318 (1973); Eyer, W.W., The Sale Leasing and Financing of Aircraft, 45 Journal of Air Law and Commerce 217 (1979-1980).

3.

AN IMPORTANT AND NOVEL QUESTION OF FEDERAL LAW IS ALSO PRESENTED BY THIS CASE: CAN A FEDERAL CLAIM FOR CIVIL DAMAGES BE MAINTAINED AGAINST A PURCHASER WHO FAILS TO RECORD HIS CONVEYANCE BY A PARTY WHO, IN RELIANCE UPON THE FAA REGISTER, PURCHASES OR EXTENDS CREDIT WITHOUT KNOWLEDGE OF THE UNRECORDED PURCHASE?

If Section 1403 does not preempt state law insofar as state law would permit conveyance of title to aircraft without recording, then the reliability and usefulness of the FAA central registry will vanish unless some sanction is imposed against the non-recording party. Petitioner Philko submits that it should be permitted to maintain a federal claim against Shacket for damages to the extent such damages were proximately caused by Shacket's failure to record his conveyance. The criteria for implication of such a federal claim as expressed in *Cort v. Ash*, 422 U.S. 66 (1975) are clearly met here:

First, Philko, being a third party without notice of Shacket's transaction, who relied on the information at the FAA registry and the original bills of sale, clearly is one of the class for whose especial benefit Section 1403(c) was enacted;

Second, the legislative history of the FAA recording provisions indicates that Congress intended to make mandatory the requirement of recording instruments affecting aircraft title. Senate Commerce Committee Report No. 1060, which accompanied the bill subsequently enacted as 49 U.S.C. Sec. 1406 contains the most recent pronouncement of the legislature on the FAA recording requirements:

> The fact that the determination of the validity of aircraft conveyances involved extremely cumbersome and complex procedures was recognized by

> the Congress when it originally enacted the Civil Aeronautics Act of 1938. That act contained a provision which provided for the establishment of a central national recording system for all instruments affecting title to or interest in civil aircraft of this country. This provision was incorporated in section 503 of the Federal Aviation Act of 1958 substantially without change. It continued the previously established recording system and provides that no conveyance or instrument affecting aircraft shall be valid until filed for recordation except as to parties to the instrument or persons with actual knowledge of its existence. When the instrument has been filed for recordation under the law, all persons are deemed to have notice of its existence and its effect on title to the property covered thereby. Consequently, to determine whether there are any encumbrances on the aircraft, it is only necessary to consult the central file.

If the legislative intent is to create a reliable central register it follows that parties dealing with aircraft titles should not be permitted to disregard the federal statute with impunity. If the failure to record does not vitiate a party's interest (as the Court below held) it follows that the party who is damaged by relying on the FAA register should be entitled to recover from a prior purchaser or encumbrancer who fails to record. An action for civil damages is therefore implicit in the mandatory nature of the FAA recording requirements.

Third, an action for civil damages is fully consistent with the Act. Congress has given persons who deal with aircraft the right to rely upon the status of title at the FAA register. A civil action for damages is necessary to effectuate the Congressional plan of providing a comprehensive central registry for aircraft titles. Such a cause of action will insure compliance with the statute.

Fourth, the claim for damages for failure to record pursuant to Section 1403(c) is not the type of claim which can be relegated to state law because the recording requirement does not arise under state law. A state court could employ the doctrine of estoppel to preclude a non-recording party from asserting title, but if the failure to record does not affect such party's title (as the Court below found) the principle of estoppel does not afford an aggrieved party any affirmative relief. Only a federal claim under Section 1403(c) will give a remedy to a party injured by the failure to record.

The law will not suffer a wrong without a remedy. If Philko has the right to rely on the status of title as shown by the FAA registry, but cannot achieve good title in reliance upon it, then at least Philko should be entitled to a remedy of damages against the party whose nonfeasance caused the loss. It is clearly foreseeable that if the original bills of sale to an aircraft are left in the hands of the seller that the seller may attempt to re-sell or encumber the plane. In such case the party who fails to record, as the federal statute mandates, should rightfully bear the consequences. Otherwise the federal recording statute is itself the instrument through which fraud can be perpetrated. Such a result cannot be condoned.

4.

SHACKET SHOULD BE ESTOPPED FROM CLAIMING TITLE TO THE AIRCRAFT.

Plaintiff Shacket could have prevented the fraud on Philko from occurring if he had demanded the original bills of sale from Smith Inc. at the closing of his purchase. Since Shacket by his own actions created the facts upon which Smith Inc. was able to demonstrate a

clear chain of title, Shacket should be estopped from asserting any claim to the aircraft Philko purchased.

CONCLUSION

For these reasons, a writ of certiorari should issue to review the judgment and opinion of the Seventh Circuit.

Respectfully submitted,

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APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

No. 81-1249

MAURICE SHACKET and SYLVIA SHACKET,

Plaintiffs-Appellees,

v.

PHILKO AVIATION, INC.,

Defendant-Appellant.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.
No. 78 C 4284—**Milton I. Shadur**, *Judge.*

ARGUED JANUARY 4, 1982—DECIDED JUNE 22, 1982

Before PELL, *Circuit Judge*, MARKEY, *Chief Judge*,* and SPRECHER, *Circuit Judge*.**

MARKEY, *Chief Judge*. Appeal from a judgment of the district court for the Northern District of Illinois declaring title to an aircraft by way of summary judgment granted to Maurice and Sylvia Shacket. We affirm.

* Howard T. Markey, Chief Judge of the United States Court of Customs and Patent Appeals, is sitting by designation.

** Judge Robert A. Sprecher was present at oral argument and at the post-argument conference but was unable to review the opinion before his death.

Background

In April 1978, Roger Smith Aircraft Sales, Inc. (Smith Aircraft) sold a new, custom-built Piper Navajo aircraft, registration number N78MS, to Maurice and Sylvia Shacket, who took possession at that time. Subsequently, Smith Aircraft purported to sell the same aircraft to Philko Aviation Company (Philko), the "sale" being financed by Sandwich State Bank (Bank), which purported to take a security interest in the aircraft.

The Shackets brought suit for a judgment declaring their right of ownership in the aircraft. The Shackets and Philko filed motions for summary judgment. Judge Shadur granted summary judgment in favor of the Shackets. Philko's motion for reconsideration was denied, but the court modified its prior opinion respecting certain factual matters and terminology.

Background

Maurice Shacket, a private pilot and aircraft owner for many years, and his wife Sylvia, contracted with Smith Aircraft in 1977 to buy the aircraft for $126,000 plus the trade-in of an aircraft valued at $120,000, giving a check for $20,000 as a down payment. Smith Aircraft, engaged in buying and selling used aircraft, contracted to purchase the new aircraft from Clark Aviation, Inc. (Clark), a Piper franchisee. The Shackets were aware of the arrangements between Smith Aircraft and Clark, and were in contact with Kenneth Rittenhouse, Clark's president and principal shareholder, regarding customizing of the aircraft before final delivery. Citing financial problems Clark had with Smith Aircraft, Rittenhouse requested that he be present at the closing and advised the Shackets not to pay Smith Aircraft unless he was there. The Shackets agreed.

Before the closing, Smith Aircraft located a customer for its resale of the trade-in aircraft. The Shackets relinquished possession of that aircraft for delivery to that customer, keeping the title papers as presumed security for the transaction.

At the closing, Mr. Shacket asked Rittenhouse whether it was all right to close the purchase and Rittenhouse said it was, though Rittenhouse had not yet received full payment from Smith Aircraft. The Shackets then endorsed two cashiers' checks, aggregating $106,000, in favor of Smith Aircraft. Rittenhouse showed the Shackets the aircraft and handed them various manuals, the certificate of airworthiness, and the keys. The Shackets subsequently returned home in the new aircraft and have retained possession ever since.

The present controversy is in part generated by failure of Roger Smith, president of Smith Aircraft, to give the Shackets all the proper bills of sale reflecting the chain of title in the aircraft, and in part by Smith's "sale" of the same aircraft to two different parties. Telling the Shackets that the legal title could not be delivered at closing because of uncompleted clerical work, Smith supplied the buyer's copy of the bill of sale, and photocopies of bills of sale covering prior transfers of the aircraft and said he would "take care of the paperwork." The Shackets understood that to mean Smith would record the bills of sale as part of the "paperwork." No recording of the Shackets' interest was accomplished.

Through Smith, Edward McArdle learned of an aircraft operation (Philko) for sale at the Aurora Municipal Airport. McArdle purchased Philko, becoming its president and principal stockholder, and leasing its operations to Smith Aircraft. Under the lease arrangement, Smith Aircraft would continue existing operations under Philko's name, accounting to Philko for all expenses and receipts.[1] Smith Aircraft was permitted to use Philko's buildings for Smith Aircraft's used aircraft sales and charter business. McArdle extended his personal credit and the credit of his companies to assist

[1] The Philko operations included the sale of oil and gasoline, operation of a flight school, aircraft maintenance and repair, and the sale of new aircraft.

Smith Aircraft, guaranteeing $100,000 of its $500,000 line of credit and loaning it $80,000. When Smith approached McArdle concerning the Piper aircraft in question, Smith Aircraft owed Philko $60,000 on the loan.

Two days after closing with Shackets, Smith told McArdle he needed $152,000 to complete purchase of the same aircraft he had already sold and delivered to the Shackets, telling him the aircraft was to be sold to Krueger Aviation Inc., a California corporation (Krueger). Smith said the Bank would not advance funds to complete the transaction because an advance would exceed his line of credit and showed McArdle a copy of a purported purchase order signed by Krueger. Smith told McArdle the sale would enable him to erase the $60,000 debt to Philko.

After McArdle and the Bank examined the original prior bills of sale exhibited by Smith, and checked the title against Federal Aviation Administration (FAA) records, McArdle agreed that Philko would take title to the plane from Smith Aircraft. All the proceeds of the Krueger sale would be credited to Smith Aircraft ($152,000 being repaid to the Bank, $60,000 being applied to payment of the Philko loan, and the balance going to Smith Aircraft). The Bank subsequently recorded with the FAA the bill of sale to Philko and the Bank loan agreement, though Philko never received physical possession of the Piper aircraft.

Issues

1. Did the district court err in concluding that state law governs validity of the transfers of the aircraft?

2. Did the district court err in concluding that under state law the Shackets obtained title to the aircraft as a result of their purchase from Smith Aircraft?

3. Did the trial court err in concluding that under state law Philko did not obtain title to the aircraft?

4. Were there genuine issues of material fact sufficient to preclude grant of summary judgment to the Shackets?

OPINION

1. *Effect of the Shackets' Failure to Record*

Under the Federal Aviation Act of 1938 (Act), 49 U.S.C. §1401 et seq., Congress established a system for national registration of conveyances and encumbrances affecting aircraft. Registration entails filing an application for registration with the FAA in Oklahoma City, disclosing prescribed information about the owner, evidence of ownership, and a filing fee. Upon acceptance of the application, the interest is recorded and a certificate of registration issued. Section 1403 of the Act recites the broad range of conveyances included within the scope of the recording system and further provides at section c:

> §1403(c) No conveyance or instrument, the recording of which is provided for by [§1403(a)] shall be valid in respect of such aircraft, aircraft engine or engines, propellers, appliances, or spare parts against any person other than the person by whom the conveyance or other instrument is made or given, his heir or devisee, or any person having actual notice thereof, until such conveyance or other instrument is filed for recordation in the office of the Administrator.

Philko argues that §1403(c) preempts state law and invalidates any conveyance of an aircraft without recordation. Any federal preemption however is limited by the terms of 49 U.S.C. §§1401(f) and 1406. The former provides that the FAA issued certificate of registration shall not be evidence of ownership in any proceeding where ownership is in issue. Congress indicated a further deference to state law in 1964 when it enacted §1406.

> §1406 The validity of any instrument the recording of which is provided for by section 1403 of this title shall be governed by the laws of the State, District of Columbia, or territory or possession of the United States in which such instrument is delivered . . . .

The extent to which the Act effects priorities between claimants under successive transactions involving the same aircraft must therefore be limited. In *Sanders v. M.D. Aircraft Sales, Inc.*, 575 F.2d 1086 (3rd Cir. 1978), the court noted:

> [T]here has been preemption by federal law only to the limited extent that Congress has sensibly federalized choice of law, thereby freeing aircraft financing from the forum shopping which the rule of *Klaxon Co. v. Stentor Elec. Co.*, 313 U.S. 487, 61 S. Ct. 1020, 85 L. Ed. 1477 (1941), might otherwise produce.

Id. at 1088; also quoted in *Blitzer-Croft Motors, Inc. v. Pioneer Bank & Trust Co.*, 82 Ill. App. 3d 1, 401 N.E. 2d 1340, 1345 (1980).

Since the enactment of §1406, numerous courts have adopted the view that the Act is subject to UCC principles of good faith purchaser status, actual notice, and the rights of a buyer in the ordinary course, as Judge Shadur determined the Shackets to be.[2] Thus, though the manner of recordation and choice of law question are resolved under the Act, the underlying validity and effect of an instrument are subject to applicable state law. We therefore conclude that the Act does not preempt all state laws governing priorities among

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[2] *E.g., Sanders v. M.D. Aircraft Sales Inc., supra; Blitzer-Croft Motors Inc. v. Pioneer Bank & Trust Co., supra; Haynes v. General Electric Credit Corp.*, 582 F.2d 869 (4th Cir. 1978); *State Securities Co. v. Aviation Enterprises*, 355 F.2d 225 (10th Cir. 1968); *No. Illinois v. Biship Distributing*, 284 F. Supp. 121 (D.C. Mich. 1968); *but see, Dowell v. Beach Acceptance Corporation, Inc.*, 3 Cal. 3d 544, 475 P.2d 401 (1970).

security interests, and that the interests of the parties in the aircraft in this case must be determined by reference to state law.

2. *The Shackets' Interest Under State Law*

The state law applicable to the sale of goods in Illinois is the Uniform Commercial Code (UCC).[3] UCC §1-201(9) defines a buyer in the ordinary course of business.

> (9) "Buyer in ordinary course of business" means a person who in good faith and without knowledge that the sale to him is in violation of the ownership rights or security interest of a third party in the goods buys in ordinary course from a person in the business of selling goods of that kind but does not include a pawnbroker. "Buying" may be for cash or by exchange of other property or on secured or unsecured credit and includes receiving goods or documents of title under a pre-existing contract for sale but does not include a transfer in bulk or as security for or in total or partial satisfaction of a money debt.

Having paid Smith Aircraft $126,000 in cash and turned over possession of a trade-in aircraft, the Shackets are clearly "buyers" under §1-201(9) and purchasers who have given value under §§1-201(32), (44). As Judge Shadur noted, the good faith of the Shackets was demonstrated when they specifically asked Rittenhouse whether it was alright to close on the purchase, and were told that it was. The Shackets were under no obligation to monitor Smith Aircraft's financial arrangements with Clark, and therefore their failure to know of Smith Aircraft's outstanding financial obligations to Clark raises no issue of good faith.

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[3] Under §1406 of the Act, Illinois law governs the transaction between Clark, Smith Aircraft, the Shackets, Bishop and Philko. In each case the transaction took place, and the instrument evidencing the respective interests was delivered, in Illinois.

It is unquestioned that Clark had good title to the new aircraft, was in the business of selling new aircraft, and entrusted possession of the new aircraft to Smith Aircraft. That Smith Aircraft was only in the business of selling used aircraft, as Philko asserts, does not detract from its ability to transfer the good title of Clark to the Shackets. Under UCC §2-403(2) the effect of entrustment of goods to one who deals in goods "of that kind" is to pass all rights of Clark to the Shackets, as buyers in the ordinary course of business.[4] The term "goods of that kind" is not limited to the same goods but encompasses goods of the same fundamental nature. That Smith Aircraft was in the business of selling aircraft on a commercial basis is sufficient to permit Smith Aircraft to pass good title to a buyer in the ordinary course.

Illinois case law illustrates the effect of §2-403(2). In *Coffman Truck Sales v. Sackley Cartage Co.*, 58 Ill. App. 3d 68, 373 N.E.2d 1026 (1978), the Illinois Appellate Court applied that section, holding that a buyer from a resale dealer who purchases in an ordinary transaction is a buyer in due course and therefore obtains title of the first dealer, even if the resale dealer failed to remit payment for the goods to the first dealer.

Similarly, the Shackets, as buyers in the ordinary course from Smith Aircraft, obtained the title entrusted by Clark to Smith Aircraft, notwithstanding any difficulties in the title of Smith Aircraft.[5]

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[4] UCC §2-403(2) provides: "Any entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business." *See also, Bank of Hendersonville v. Red Baron Flying Club, Inc.*, 571 S.W.2d 152 (Tenn. App. 1977), *cert. denied* (Tenn. 1978), *cert. denied*, 439 U.S. 1089 (1979), holding that the entrustment doctrine applies to sales of aircraft.

[5] As Judge Shadur noted, the Shackets could also predicate good title under UCC §2-403(1) as good faith purchasers for value who, upon delivery of the goods, have acquired good title notwithstanding any voidable title in Smith Aircarft.

Philko's argument that Smith Aircraft acted as an agent of the Shackets (and therefore could not have passed good title to them) ignores the evidence. In denying a motion to modify judgment, Judge Shadur quoted from his own opinion:

> [T]he mark of an agency relationship here would be that "if Smith Aircraft were acting as an agent and not as a principal for its own account, the purchase transaction with Clark, including the price of the aircraft as negotiated by Smith, would have been for the direct benefit of Shacket". . . . If an *agent* makes a deal for his principal, the price that the agent commits for is the price the *principal* pays. That was plainly not so here, where Smith Aircraft was plainly dealing for its own account in the purchase from Clark Aircraft.

Accordingly, we find no error in Judge Shadur's determination that the Shackets obtained title to the aircraft as a result of the purchase from Smith Aircraft.

3. *Philko's Interest Under State Law*

Philko's claim under state law is twice flawed: it cannot be a buyer in ordinary course; and its failure to take possession precludes acquisition of good title as a good faith purchaser for value.

"Buying" under UCC §1-201(9) specifically excludes transfers "as security for or in total or partial satisfaction of a money debt." Thus, a person may give "value" as defined in UCC §1-201(44) (which specifically includes acquiring rights "as security for or in total or partial satisfaction of a pre-existing claim"), yet not be a "buyer" for purposes of UCC §1-201(9).

Smith Aircraft owed Philko $60,000 on its $80,000 loan. Smith told Philko he could not obtain sufficient credit to buy the new aircraft, but if Philko would supply the purchase price, Smith Aircraft would resell the aircraft and repay both the purchase price and the $60,000 balance. As the district court noted:

> Thus it is plain from his own testimony McArdle had no interest in the sale price to be paid by Krueger Aviation, except to make sure it was adequate to pay the bank loan and the $60,000 balance owed to Philko. That is the conclusive hallmark of a *credit* transaction not a purchase. . . . Philko was acting to accommodate Smith Aircraft (though its purpose of course was the legitimate one of obtaining repayment of an existing debt), not to take the risks of profit and loss that are the essence of a true purchase. . . . Philko's acquisition of title was by way of security.

Because "buying" does not include a transfer as security, Philko cannot be a "buyer" in the ordinary course".[6]

Whether Philko has the status of a good faith purchaser is of no consequence. Such status of itself cannot be the basis for good title in this case absent possession of the aircraft. At the time of the "sale" to Philko, Smith Aircraft had neither title to nor possession of the aircraft. Consequently, Philko could not under UCC §2-403(1)[7] acquire good title from Smith Aircraft, whether

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[6] Moreover, there was at the time of the "sale" to Philko no entrusting of possession in Smith Aircraft to predicate the passage of title to Philko under UCC §2-403(2), *supra* at n.5.

[7] UCC §2-403(1) provides:

> (1) A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though
>
> (a) the transferor was deceived as to the identity of the purchaser, or
>
> (b) the delivery was in exchange for a check which is later dishonored, or
>
> (c) it was agreed that the transaction was to be "cash sale," or
>
> (d) the delivery was procured through fraud punishable as larcenous under the criminal law.

any voidable title that may have arguably accrued to Smith Aircraft because it retained the title papers or otherwise.

Accordingly, under state law, Philko acquired no title to the aircraft.

4. *No Genuine Issue of Material Fact*

Rule 56(c), Fed. R. Civ. P., provides that summary judgment "shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Philko asserts that six issues of material fact exist: (1) whether the Shackets were guilty of bad faith; (2) whether the Shackets were buyers in the ordinary course of business; (3) whether Smith Aircraft was in the business of selling goods of that kind; (4) whether there was an agency relationship between Smith Aircraft and the Shackets; (5) whether title to the trade-in aircraft passed; and (6) whether the proceeds from the proposed sale to Krueger inured to the benefit of Philko or Smith Aircraft.[8]

Respecting (1) and (5), Philko questions the honesty of the Shackets, suggesting that there might have been additional terms in the Shackets-Smith Aircraft transaction that were not stated in the record, noting particularly the Shackets' retention of title to the trade-in aircraft pending delivery of title to the new aircraft. Philko suggests that the Shackets and Smith Aircraft might have agreed that title would not pass until the exchange of the legal title papers. That conjecture, however, is an insufficient response to the direct evidence demonstrating the Shackets' good faith at the time of the transaction, as indicated by payment in full,

[8] Mere allegations or denials in the pleadings are insufficient to establish genuine issues for trial. Rule 56(e) Fed. R. Civ. P.

upon approval of Rittenhouse, and their understanding that the "paperwork" was being completed by Smith Aircraft. No issue of material fact touching the Shackets' good faith has been shown to exist.

Assertions (2), (3), and (4), relate not to fact issues but to legal conclusions drawn in this case from undisputed evidence in the record. Philko's suggestion that factual disputes may underlie resolution of those issues is a poor substitute for record evidence that would conflict with Judge Shadur's determinations. Philko's assertions (2), (3), and (4) fail to demonstrate existence of any issue of material fact.

Assertion (6) was resolved in the testimony of McArdle.

> [Smith said] that he had sold an airplane to Krueger Aviation . . . for $280 or $290 [thousand dollars] . . . [Smith] said that he wanted—he had gone to the bank and requested financing for the balance of the purchase of $152,000. And the bank told him that if they loaned him $150,000 it would be beyond his line of credit, words to that effect. . . . and he said that if I purchased this airplane, when this buyer, Krueger Aviation, was going to purchase—would purchase the thing from me, witnessed the fact that I had a contract here signed by Krueger, I would receive my $152,000 or whatever it was plus the $60,000 from the proceeds of the sale. And of course the difference—it would be profit to him and Krueger, I guess.

Philko points to no evidence in the record to contradict the obvious conclusion that, at least in McArdle's mind, Smith Aircraft was to receive all of the profit on the purported resale to Krueger. Philko's assertion (6) therefore fails to demonstrate any issue of material fact sufficient to preclude summary judgment to the Shackets.

There being no error in Judge Shadur's grant of summary judgment to the Shackets, the same is affirmed.

A true Copy:
Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

APPENDIX B

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

MAURICE SHACKET and
SYLVIA SHACKET,
Plaintiffs,

v.

ROGER SMITH AIRCRAFT
SALES, INC., et al.,
Defendants.

PHILKO AVIATION, INC.,
Counter-Plaintiffs,

v.

MAURICE SHACKET, et al.,
Counter-Defendants.

SANDWICH STATE BANK,
Counter-Plaintiff,

v.

MAURICE SHACKET, et al.,
Counter-Defendants.

No. 78 C 4284

DECLARATORY JUDGMENT ORDER

This matter coming upon to be heard for entry of declaratory judgment order, the Court having rendered a Memorandum Opinion and Order dated September 22, 1980, which granted plaintiffs Maurice and Sylvia Shacket's motion for summary judgment on Count I of the complaint against Philko Aviation, Inc. and Sandwich State Bank and further granted summary judgment for Philko Aviation, Inc. and Edward J. McArdle on Count II of the complaint; and a default judgment against the other defendants, Roger Smith and Roger Smith Aircraft Sales, Inc., having been entered on December 18, 1980 and the Court having rendered a Memorandum Opinion and Order dated January 19, 1981, denying in principal part the motion of Philko Aviation, Inc. for modification of its September 22, 1980 Memorandum Opinion and Order; and the Court being fully advised in the premises;

It is hereby ordered, adjudged and decreed that:

1. Judgment is hereby entered in favor of plaintiffs Maurice and Sylvia Shacket and against defendants Philko Aviation, Inc. and Sandwich State Bank upon Count I of the Complaint, with costs as to said Count to be allowed to plaintiffs.

2. Plaintiffs Maurice and Sylvia Shacket are the true and lawful owners of all right, title and interest in and to a certain Piper PA-31 aircraft, Serial Number 31-7812074, with a FAA Registration No. N78 M.S. (the "Aircraft").

3. Defendant Philko Aviation, Inc. does not have any right, title or interest in or to the Aircraft, and the Bill of Sale recorded by Philko Aviation, Inc. as owner as FAA Document No. C-172546 is a nullity.

4. Defendant Sandwich State Bank does not have any right, title or interest in or to the Aircraft, and Trust Receipt-Security Agreement filed by Sandwich State Bank as FAA Document No. 172547 is a nullity.

5. Defendants Philko Aviation, Inc. and Sandwich State Bank, their directors, officers, shareholders, agents and employees and all persons acting through and under said defendants are hereby enjoined from directly or indirectly interfering with, converting, hypothecating or otherwise affecting the right, title and interest of plaintiffs Maurice and Sylvia Shacket in and to the Aircraft.

6. Plaintiffs Maurice and Sylvia Shacket are authorized to file a certified copy of this Declaratory Judgment Order with the appropriate agencies to record their ownership rights in and to the Aircraft.

7. Judgment is hereby entered in favor of defendants Philko Aviation, Inc. and Edward J. McArdle and against plaintiffs Maurice and Sylvia Shacket upon Count II of the Complaint, with costs as to said Count to be allowed to said defendants.

8. Judgment is hereby entered in favor of counterdefendants Maurice and Sylvia Shacket upon the Counterclaims filed by counterplaintiffs Philko Aviation, Inc. and the Sandwich State Bank, with costs as to said Counterclaims to be allowed to said counterdefendants.

/s/ Milton I. Shadur
United States District Judge

Date:

APPENDIX C

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

MAURICE SHACKET and SYLVIA SHACKET,
Plaintiffs,
v.
ROGER SMITH AIRCRAFT SALES, INC., et al.,
Defendants.

PHILKO AVIATION, INC.,
Counter-Plaintiffs,
v.
MAURICE SHACKET, et al.,
Counter-Defendants.

SANDWICH STATE BANK,
Counter-Plaintiff,
v.
MAURICE SHACKET, et al.,
Counter-Defendants.

No. 78 C 4284

MEMORANDUM OPINION AND ORDER

This action involves a dispute over the ownership of a Piper Navajo airplane sold twice by defendants Roger Smith ("Smith") and Roger Smith Aircraft Sales, Inc. ("Smith Aircraft").[1] Plaintiffs Maurice and Sylvia Shacket ("Shackets"[2]) are in possession of the plane and have asked this Court in Count I for a declaratory judgment that they own the plane free of any claims of defendants. Defendant Philko Aviation Company ("Philko") has counterclaimed asserting its ownership of the plane. Defendant Bank has claimed a lien if the plane is owned by Philko. Shackets have also alleged in Complaint Count II that Philko aided Smiths in seeking to defraud Shackets of their interest in the plane and that all defendants have engaged in fraudulent conversion. Counterclaims have been filed by Philko and Bank.

Shackets and Philko have filed cross-motions for summary judgment on Count I, and Philko and defendant Edward McArdle ("McArdle"), its president and principal shareholder (through a holding company), have moved for summary judgment on Count II. For the reasons stated in this memorandum opinion and order, Shackets' motion for summary judgment as to Count I is granted (and Philko's is denied), and the Philko-McArdle motion for summary judgment as to Count II is also granted.

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[1] Throughout the transactions involved in the case Smith was the president and principal shareholder of Smith Aircraft, whose business was the buying and selling of aircraft. It was thinly capitalized and heavily financed. It had in late 1977 and early 1978 sold three other aircraft out of trust, a matter discovered by defendant Sandwich State Bank ("Bank") in May 1978 when it made a floor plan check on the five aircraft (including the three that proved to have been improperly sold) it was currently financing for Smith. For convenience, Smith and Smith Aircraft are sometimes collectively referred to in this memorandum opinion as "Smiths."

[2] Maurice Shacket ("Shacket") was involved in all of the negotiations and closed the transaction on behalf of plaintiffs.

Facts

1. *The First Sale.*

Shacket, a private pilot and owner of aircraft for many years, contracted with Smith Aircraft in 1977 to buy a custom-built Piper Navajo plane for $126,000 plus the trade-in of a plane currently owned by Shacket, the wholesale value of which was $120,000. Shacket paid $20,000 down on the purchase price upon signing the contract with Smith Aircraft. Smith Aircraft in turn contracted to acquire the plane from Clark Aviation, Inc. ("Clark," the Piper franchisee for the area), an arrangement of which Shacket was aware. Before the closing of Shacket's purchase of the plane, Smith located a customer for his resale of the trade-in aircraft, and Shacket turned over possession of the trade-in aircraft for delivery to Smith's customer. After completion of the necessary work on the Piper Navajo to meet Shacket's specifications, the closing was set for April 18, 1978.

As of the closing date Smith Aircraft had not been able to pay Clark for the plane to be sold to Shacket,[3] but that did not prevent the closing from taking place on April 19. Closing involved a meeting at an airport attended by Shacket, Smith and Clark's president and principal shareholder, Kenneth Rittenhouse ("Rittenhouse"). Rittenhouse had previously told Shacket of financial problems Clark had encountered with Smith Aircraft (the delivery of one, or perhaps two, NSF checks). As a special request Rittenhouse had told Shacket that he wanted to be present at the closing and that Shacket should not pay Smith Aircraft for the plane unless Rittenhouse were there.

At the closing Shacket asked Rittenhouse whether it was all right to close the purchase of the plane and

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[3] There is a dispute as to whether Smith paid any money at all to Clark. Shackets allege that $3,000 was paid, with all subsequent checks being returned for insufficient funds. Defendants claim that all of the checks from Smith to Clark were returned for insufficient funds. That dispute does not raise any issue as to a material fact.

Rittenhouse said it was. Shacket then endorsed two cashiers' checks aggregating $106,000 in favor of Smith Aircraft. Rittenhouse and Smith showed Shacket the plane, turned over to Shacket various manuals and the certificate of airworthiness and handed the keys to Shacket. Shacket flew the plane to Detroit and has had possession ever since.

Essentially the problem in this case has been generated by Smith's failure at the closing to give Shacket all the proper bills of sale reflecting the chain of title to the plane. Smith did give Shacket the buyer's copy of the bill of sale from Smith Aircraft to Shacket, together with photocopies of the bills of sale covering prior transfers of the plane, and told Shacket that Smith would "take care of the paperwork." Shacket understood that to include an undertaking by Smith to record the bills of sale as part of the "paperwork."

There is a central registration system for aircraft conveyances under the Federal Aviation Act (the "Act"). Such registration requires the original bill or bills of sale covering the chain of title. After the closing Shacket made several attempts to get the prior bills of sale from Smith but was unsuccessful. Thus Shacket was unable to register his purchase with the Federal Aviation Administration (the "FAA").

2. *The Second Sale.*

Before the events described in the prior section, McArdle had been pressuring Smith to repay the remaining balance of $60,000 on Philko's $80,000 loan made to Smith Aircraft in December 1977. On April 18, 1978, the same day that Shacket arrived in Aurora for his closing the following day, Smith came to McArdle and represented that he had contracted with Clark to purchase a plane (which was in fact the same plane about to be paid for by and delivered to Shacket) for resale to a third party, Krueger Aviation. Smith claimed to have tried to borrow $152,000 from Bank on the plane but to have been refused because that would have exceeded his line of credit with Bank.

After McArdle and Bank had examined the original bills of sale that Smith exhibited, McArdle agreed that Philko would take title to the plane from Smith Aircraft, enabling it to obtain the same $152,000 loan from Bank to be secured by that title, and then to complete Smith Aircraft's previously committed sale to Krueger Aviation. All the proceeds of the Krueger sale would be credited to Smith Aircraft (with $152,000 of those proceeds being contemporaneously repaid to Bank, $60,000 being applied in payment of the prior Philko loan to Smith Aircraft, and the balance belonging to Smith Aircraft).

On April 22, 1978, just two days after the Shacket transaction, Philko executed its note for $152,000 to Bank, which in turn issued its cashier's check for that amount to Clark. Bank showed the remitter on the cashier's check as "Roger Smith Aircraft Sales, Inc. (Philko Aviation, Inc.)." On April 24, 1978 Smith Aircraft executed a bill of sale to Philko (the same date appears on all of Bank's security documents other than the Philko note to Bank, which was dated April 22).

At that point Bank had all of the original bills of sale establishing the paper chain of title in its possession (a series of bills of sale running from Piper Aviation to North States Aviation [the Piper distributor for the area] to Clark to Smith Aviation to Philko). All those documents were then transmitted by Bank to the Federal Aviation Administration for recording. Bank delayed that transmittal for a period of time. Its reason for delay was that where another sale of an aircraft is expected to be made, the administrative delay in recording earlier bills of sale can cause problems in implementing the subsequent sale. In any case, the present situation is that Shacket has the physical possession of, while Philko has the FAA registered title to, the plane.[4]

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[4] From the facts stated by the parties, it is the Court's understanding that the Krueger Aviation transaction promised by Smith never proceeded, but that fact is not critical to decision of the pending motions.

3. *Prior Relationships Among the Defendants.*

McArdle, the owner of a large number of corporations through his holding company McArdle, Ltd., first met Smith in 1976 or 1977 when McArdle was contemplating the purchase of corporate aircraft. In about April 1977 Smith, who wanted to acquire a new base of operations, learned about the availability for sale of the corporation that was lessee of the Aurora Airport from the City of Aurora. Because he didn't have funds to make the deal himself but regarded it as a good buy, Smith approached McArdle as a possible financial backer. Smith proposed that McArdle purchase the operation and lease it to Smith Aircraft on terms that would make it a good investment.

McArdle investigated Smith Aircraft's financial viability (including having an audit performed). He found that Smith Aircraft did a large volume of business but lacked operating capital and needed added credit to carry on its purchases of planes. Having satisfied himself on that score, McArdle caused one of his corporations to purchase the Airport lessee (which became Philko by corporate merger) and caused Philko contemporaneously to sublease the Airport to Smith Aircraft for a five year term.

Smith Aircraft became more than a sublessee of Philko as a result of the April 1977 transaction, although the document the parties executed was termed a "Lease Agreement." In its sublessee capacity, Smith Aircraft agreed to make all the rental payments to the City of Aurora, and to perform all other obligations imposed on Philko as lessee, under the leases from the City; that much of course represented a conventional lessor-lessee relationship. But the parties also contracted for Smith Aircraft to conduct several related businesses *in Philko's name*, to be carried out by Smith Aircraft's own personnel:

1. the purchase and sale of aviation fuel and lubrication oils;
2. the operation of the flight school at the airport;

3. rendering of maintenance services; and
4. sales of *new* Piper aircraft.

Smith Aircraft was "permitted to do business *in its own name* as a purchaser and seller of *used* aircraft." For a period of approximately 1½ years thereafter Philko purchased aircraft for its corporate use from Smith Aircraft (which purchased such aircraft for its own account and resold them to Philko), and Smith Aircraft also carried out the sale of Philko's aircraft inventory in the same manner (it was not paid a commission as though it were a broker). During the same period McArdle also entered into two major financing transactions to assist Smith Aircraft (in addition to the April 1978 transaction discussed above in "The Second Sale"):

1. the guaranty of $100,000 of Smith Aircraft's $500,000 line of credit with Commercial Credit Equipment Corporation, entered into at the same time as the April 1977 lease and other arrangements; and
2. the loan of $80,000 in December 1977, secured by the personal guaranties of Smith and his wife and by their pledge of the stock of Smith Aircraft.

Indeed, one portion of the April 1977 "Lease Agreement" was (taken in the light *most favorable* to Philko) still another financing of—that is, an extension of credit to—Smith Aircraft's operations. This was the provision under which Smith Aircraft was (1) to "provide its personnel for the operation of [Philko's] sale of aviation fuel and lubrication oils, which operation shall be conducted only in the name of [Philko] as provided below," and (2) to remit to Philko, within ten days after the end of the month of *sale* of such materials, the cost of all such materials purchased in Philko's name plus the amounts due to the City of Aurora by reason of such sales.

In still another aspect of the Smith-McArdle relationships, McArdle proposed in December 1977 to purchase the stock of Smith Aircraft, and Philko made a payment of $5,000 as an advance toward such possible

purchase. That transaction was not consummated and the $5,000 was repaid early in 1978, so that at the time of the April 1978 transactions Smith still owned the stock of Smith Aircraft subject to the pledge to Philko.

As for the Bank-Smiths relationships, Smith Aircraft had established a floor plan arrangement with Bank beginning in 1974. As already stated, Smith's capital investment in Smith Aircraft has always been small, and Smith Aircraft experienced intermittent cash shortages from 1972 through 1978. Smith Aircraft's out-of-trust sale of aircraft financed by Bank has also been referred to earlier. Bank itself was experienced in airplane financing transactions, having handled about 100 since 1974 and having carried on two floor plan arrangements since 1974 involving substantial numbers of aircraft.

We turn then to the parties' respective motions in light of the facts as just summarized.

Shackets' Status as Good Faith Purchasers

Ordinarily the law applicable to the sale of goods is the UCC (the Illinois version, Ill. Rev. Stat. ch. 26, §§ 1-101 ff., is hereinafter cited to the UCC section numbers). Here however the threshold question is whether the registration provisions of the federal Act for aircraft conveyances preempt the UCC for purposes of determining title questions relating to aircraft. From its inception in 1938 the Act was intended to unify title registration for airplanes and eliminate the confusing array of state statutes (a purpose especially appropriate in light of the great mobility of the subject matter). In dealing with priorities between claimants under successive transactions involving the same aircraft, courts have reached differing results as to the precise effect of the Act. Professor Gilmore has said that its provisions "obviously amount to a good deal more than a recording system . . . but are still a good deal less than a comprehensive coverage of security interests in aircraft. . . ." 1 Gilmore, *Security Interests in Personal Property* 546-48 (1st ed. 1965).

But as between the parties to a transaction themselves, there appears to be no question that state law

governs to determine the validity of the transfer from Smith Aircraft to Shackets.[5] We therefore turn to the UCC.

In that respect the first question is whether the sale to Shackets was valid in view of the fact that Smith Aircraft had never paid for the airplane built by Clark. On the record as presented to the Court, the conveyancing instruments bringing title to the plane up to Clark were in existence and copies were exhibited to Shackets at the closing. In those circumstances the Smith Aircraft-Shackets transaction can be validated under the UCC either on a theory of voidable title or entrustment.

Although the general rule is that a transferor can give no better title than he has himself, UCC §2-403 provides several exceptions. Under Section 2-403(a)(c) a purchaser acquires voidable title "When goods have been delivered under a transaction of purchase . . . even though . . . (c) it was agreed that the transaction was to be a cash sale . . ." As stated in J. Fonseca and A. Squillante, *Williston on Sales* §23-13 (4th ed.):

> The basic rule of the cash sale is that the transferor purchaser from the true owner has the ability to transfer a good title to a good faith purchaser for value even though that transferor purchaser never in fact paid for the goods.

Alternatively UCC §2-403(2) states, "Any entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in the ordinary course of business." *Williston on Sales* §23-14 summarizes the principles involved:

> Entrusting has four essential elements. First, there must be an actual entrustment of the goods by the

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[5] Section 1403(c) of the Act provides that no conveyance or instrument whose recording is provided for "shall be valid in respect of such aircraft . . . against any person *other than the person by whom the conveyance or other instrument is made or given* . . ." (emphasis added). It may be noted, though the issue is not the same, that Section 1406 provides that the validity of recordable instruments is to be governed by state law.

> delivery of possession of those goods to a merchant. Second, the party who receives the entrustment of those goods must be a merchant who deals in goods of that kind. Third, that merchant who deals in goods of that kind must make a sale of those goods. Fourth, the sale which the entrusted merchant makes must be to a buyer in the ordinary course of business.[6]

On the day of the closing, President Rittenhouse of Clark flew the Piper Navajo to the airport where the closing took place. It is undisputed that Shacket asked Rittenhouse at the closing whether it was all right to pay the money to Smith Aircraft and Rittenhouse responded affirmatively. Clearly Clark, through Rittenhouse, either entrusted the goods or gave voidable title to Smith Aircraft (which was equally clearly a merchant dealing in aircraft).

Doctrines of voidable title and entrustment do not protect all purchasers. To secure good title from a party who has only voidable title, one must be a good faith purchaser for value. Similarly, to secure good title from a party who has been entrusted with goods, one must be a buyer in the ordinary course of business. UCC § 1-201(9) defines a buyer in the ordinary course of business as one who buys "in good faith without knowledge that the sale is in violation of the ownership rights or security interest of a third party. . . ." Thus to be protected by either the voidable title or the entrustment doctrine, Shackets were required to have been purchasers in good faith.

Defendants first assert that Smith Aircraft was an agent of Shackets authorized to purchase an airplane from Clark. But an agency relationship is a consensual

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[6] In the analogous area of automobile sales, it is well settled that a sale will be upheld even though the certificate of title has not been transferred. See for example *Humphrey Cadillac & Oldsmobile Co. v. Sinard*, 85 Ill. App. 2d 64 (1st Dist. 1967); *Wood Chevrolet Co., Inc. v. Bank of the Southeast*, 353 So. 2d 1350 (Ala. 1977).

agreement whereby a principal authorizes an agent to bind him to a contractual relationship; in the context of this action if Smith Aircraft were acting as an agent and not as a principal for its own account, the purchase transaction with Clark, including the price of the aircraft as negotiated by Smith, would have had to be for the direct benefit of Shacket. To support their argument defendants offer only a copy of a December 2, 1977 letter from Smith Aircraft to Shacket enclosing, as "the specifications for your 1978 C/R Navajo," a copy of a two-page Clark-Smith Aircraft document captioned "Agreement To Purchase." However, mere knowledge on the part of Shacket that Smith Aircraft had to purchase the plane to be sold to Shackets does not create an inference of an agency relationship. There was no disclosure to Shacket of Smith Aircraft's purchase price from Clark, and the financial dealings between Shacket and Smith Aircraft were wholly buyer-seller in nature. Defendants have failed to offer any evidence that, even together with reasonable inferences, might raise a material factual question as to the existence of an agency relationship.

Defendants also allege a lack of good faith on the part of Shacket. UCC §1-201(19) defines good faith as "honesty in fact in the conduct of transaction concerned." This language has been universally interpreted as mandating a subjective test based on what the party actually believed. *Walter E. Heller & Co. v. Convalescent Home*, 49 Ill. App. 3d 2 (5th Dist. 1977).[7]

Shackets assert that good faith has been proved by the following facts: Shacket paid $126,000 in cash to Smith and delivered his own former airplane as a trade-in (these factors of course also go to establish Shackets' status as purchasers); and at the closing Shacket specifically asked Rittenhouse whether it was all right

[7] Defendants' citation of *Hollywood National Bank v. International Business Machines Corp.*, 113 Cal. Reptr. 494 (2d Dist. 1974), construing the critically different California version of the UCC, is entirely inapropos.

to close the purchase and was told that it was. (Rittenhouse said nothing about Shacket's not doing so because Smith Aircraft had not paid Clark for the plane). Defendants charge bad faith on the basis of the following facts: Shacket refused to deliver the bill of sale on the trade-in plane (defendants argue that this shows Shacket's doubts about Smith's ability to convey title); Shacket tried several times after the closing to get the bill of sale from Smith; Shacket had long been aware of the registration requirement and its importance; Shacket tried after the closing to get new bills of sale from Rittenhouse; and Shacket was aware before the closing that Smith Aircraft was having trouble paying for the plane.

All of defendants' arguments based on post-closing events (Shacket's efforts to get the bill of sale from Smith or new bills of sale from Rittenhouse, and Shacket's non-delivery of a bill of sale on the trade-in plane) do not raise a genuine issue of material fact as to Shacket's good faith at the closing. Whether or not a purchaser was in good faith at the time of purchase, his inability to get the title documents needed for recording would have elicited exactly the same efforts. And the same is true of the trade-in transaction.[8] As for

[8] Shacket actually surrendered possession of his trade-in plane for delivery to Smith Aircraft's customer *before* the closing. It was *after* the closing, when Shacket could not obtain the documents on the Smith Aircraft plane, that he withheld the bill of sale on the trade-in aircraft. Defendants prove too much when they seek to draw inferences as to Shacket's good faith from the fact that the delivery of an aircraft, or the payment for a purchased aircraft, is not made contemporaneously with delivery of the conveyancing document covering the aircraft. As noted in the factual summary contained in this opinion, Philko itself turned over $152,000 to Smith Aircraft on April 22 but the bill of sale from Smith Aircraft was dated April 24 (as were the Bank's security documents other than the $152,000 note). Do defendants contend that this demonstrates Philko's lack of good faith as a purchaser—or that if Smith had unlawfully sold the plane a third time, Philko's inability to obtain the Smith Aircraft bill of sale on April 24 would have shown that it was in bad faith at the time it made payment on April 22?

Shacket's awareness of Smith Aircraft's financial problems, Shacket had no obligation to monitor Smith Aircraft's financial arrangements with Clark (a matter between those two parties), and Shacket's failure to do so does not bear on the issue of his good faith. Instead, Rittenhouse's response to Shacket at the closing that it was all right to proceed—after Rittenhouse had specifically asked to be present—conclusively rejects any lack of good faith, which the parties agree is the material fact on this issue (citing *Tumber v. Automation Design & Mfg. Co.*, 130 N.J. Super. 5, 324 A. 2d 602 (1974)).

Accordingly the Court finds that there is no genuine issue of any material fact regarding Shackets' good faith in purchasing the plane. Shackets are held to have been bona fide purchasers of the plane for value and in the ordinary course of business, and therefore to have secured good title to the plane from Smith Aircraft.

Philko's Status as a "Purchaser"

Shacket's status as a good faith purchaser does not end the matter. Defendants' motion for summary judgment argues that Philko is the sole owner of the plane (subject to the lien in favor of the Bank) even if Shacket acted in good faith. They assert that Shacket's failure to record the transaction with the FAA rendered the sale void as to third parties. Shackets, on the other hand, interpret the Act as also requiring the use of state law in determining the "*priorities*" between the two "purchasers" from Smith Aircraft. Because title to goods generally passes on transfer of possession, Shackets argue that they acquired "good title" to the plane and Smith Aircraft therefore had nothing left to convey to Philko.

In the Court's view, it is not necessary to resolve this dispute over the legal effect of recording or non-recording under the Act as between *purchasers* from the same party. That issue need not be reached because,

based on McArdle's own statements, Philko is not a "purchaser" at all.[9]

Both parties have glossed over (perhaps understandably in the case of defendants' counsel) the full statement of the key fact, acknowledged by McArdle, that the *entire* economic benefit of the Krueger Aviation purchase (not just the $60,000 used to pay off Smith Aircraft's debt to Philko) was going to go to *Smith Aircraft* not Philko. McArdle clearly stated in his deposition that all the funds from the sale, after paying the $152,000 bank loan entered into to obtain the aircraft from Clark, would inure to Smith Aircraft: $60,000 to pay off the loan from Philko, and the very substantial balance (perhaps $68,000 to $78,000) to Smith Aircraft directly.

In his deposition, McArdle said that Smith had called him to ask for a meeting. At the meeting (emphasis added):

> [Smith said] that he *had sold* an airplane to Krueger Aviation . . . for $280 or $290 [thousand dollars] . . . [Smith] said that he wanted—he had gone to the bank and requested financing for the balance of the purchase of $152,000. And the bank told him that if they loaned him $150,000 it would be beyond his line of credit, words to that effect. . . . and he said that if I purchased this airplane, when this buyer, Krueger Aviation, was going to purchase—would purchase the thing from me, witnessed the fact that I had a contract here signed

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[9] Shackets make a related contention based on the fact that "buying" under UCC §1-201(9) "does not include a transfer . . . in total or partial satisfaction of a money debt." But the Philko-Smith Aircraft transaction wasn't simply "in total or partial satisfaction of a money debt"—the $60,000 owed to Philko. That provision literally applies where no new consideration, no fresh money, is advanced by the buyer. If the Philko-Smith Aircraft transaction were in fact a purchase, the fact that in addition to the satisfaction of debt another $152,000 was paid in cash would give Philko the status of a "buyer."

> by Krueger, I would receive my $152,000 or whatever it was plus the $60,000 from the proceeds of the sale. And of course the difference—it would be profit to him and Krueger, I guess.

When in response to the last statement McArdle was asked "Profit to him and Krueger?" he responded:

> Well, profit to him [Smith]. And Krueger was a dealer and he was selling it to somebody subsequent to that. . . . I said that the papers all appear to be in order, etc., that I would sign the note and borrow the money to complete this transaction and take title to the airplane.

McArdle testified that he then called the Bank:

> I think that I verified that Roger Smith couldn't borrow the money because it would exceed his credit or something like that. . . . I think that I called from my office saying to Mr. Andrews [of the Bank] that Roger Smith was bringing out a series of documents and a note signed by me; you follow? For him to check over the documents and so forth to find out if he had all the items that he needed for to make this loan.

Thus it is plain from his own testimony McArdle had no interest in the sale price to be paid by Krueger Aviation, except to make sure it was adequate to pay the bank loan and the $60,000 balance owed to Philko. That is the conclusive hallmark of a *credit* transaction not a *purchase*.

Philko was taking title with the anticipated quick retransfer to Krueger Aviation[10] only because Bank required a credit-worthy borrower as a condition to making its loan. Philko was acting to accommodate Smith Aircraft (though its purpose of course was the legitimate one of obtaining repayment of its existing debt), not to take the risks of profit and loss that are the essence of a

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[10] This anticipation is confirmed by Andrews' statement as to the reason he did not immediately send the chain of title documents to the FAA.

true purchase.[11] This situation is no different from the frequent disputes stemming from a lender's taking absolute title to property, which the courts uniformly treat as an equitable mortgage as a matter of law. Philko's acquisition of title to the plane was by way of security. It cannot shift to Shackets the consequences of the noncompletion of the Krueger transaction that Philko had relied on in agreeing to accommodate Smith.

Under UCC §1-202(9) "buying" specifically does not include a transfer as security. Thus Philko cannot be a buyer in the ordinary course of business or a good faith purchaser under the UCC; it can only be a secured party. This case then presents a conflict between a "bona fide purchaser," who failed to record a transaction, and the holder of a subsequently recorded security interest. It appears that only one case under the Act has dealt specifically with this issue, and the case enforced the subsequent lien. *Marsden v. Southern Flight Service, Inc.*, 227 F. Supp. 411 (D.C.N.C. 1961). Although there have not been any subsequent cases that have dealt with this precise issue, the weight of subsequent authority (particularly since Section 1406 was added to the Act in 1964) has undermined the reasoning of this opinion.

Nearly all of the courts agree that a bona fide purchaser takes title free of a *prior* recorded security interest. *Bitzer-Croft Motors, Inc. v. Pioneer Bank & Trust Co.*, 82 Ill. App. 3d 1, 401 N.E. 2d 1340 (5th Dist. 1980); *Sanders v. M.D. Aircraft Sales, Inc.*, 575 F. 2d 1086 (3d Cir. 1978); *Hayes v. General Electric Corp.*, 432 F. Supp. 763 (W.D. Va. 1977), *aff'd per curiam*, 582 F. 2d 869 (4th Cir. 1978); *Northern Illinois Corp. v. Bishop Distributing*

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[11] This Court does not accept Shackets' argument that the numerous relationships between McArdle and Philko on the one hand and Smith and Smith Aircraft on the other were such as to negate Philko's good faith purchaser status as a matter of law. But the other transactions in which McArdle and Philko directly provided Smith and Smith Aircraft with, or assisted them in obtaining, credit are clearly relevant to support the uncontradicted evidence—from McArdle himself—that this transaction was another extension of credit.

Co., 284 F. Supp. 121 (W.D. Mich 1968); *Texas National Bank of Houston v. Aufdeheide*, 235 F. Supp. 599 (E.D. Ark. 1964); *contra*, *Dowell v. Beech Acceptance Corp.*, 3 Cal. 3d 544, 476 P. 2d 401 (1970), *cert. denied*, 404 U.S. 823 (1971). These courts have reasoned that while the Act pre-empts all state aircraft registration systems, it does not override basic state law principles governing priorities among conflicting interests. If a bona fide purchaser takes title free of a *prior* recorded security interest, it would follow *a fortiori* that the holder of a *subsequently* recorded security interest cannot challenge the title of a bona fide purchaser.[12]

Under the circumstances of this case, then, there is also no genuine issue of material fact on the issue of whether Philko was a good faith purchaser or otherwise entitled to priority as against Shackets. It was not, as a matter of law.

Count II of the Complaint

Shacket alleges in Complaint Count II that Smith and McArdle were business partners; that Smith had some interest in Philko; that Philko and McArdle were aware that the Shackets owned the plane when Smith Aircraft

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[12] On the issue of bona fides, it should be noted that McArdle, though intimately aware of Smith Aircraft's undercapitalization and major financial difficulties (indeed, it was due to the overdue $60,000 loan, on which McArdle had been pressing for payment, that Smith came to McArdle with the proposal regarding the plane), simply accepted without any effort at verification the story that Smith Aircraft had its equity already invested in the plane. It should be remembered that Smith Aircraft lacked possession of the plane at that time as well. Had McArdle made the single inquiry of Rittenhouse as to either the story regarding the equity investment or the plane's whereabouts, the Shackets' rights would have been disclosed immediately (unless Rittenhouse were to choose to conspire in Smith's fraudulent conduct). This Court's decision does not, however, rest on any adverse inferences from those facts (which could properly be taken if only defendants had moved for summary judgment).

executed the bill of sale to Philko; that Philko aided and abetted Smith and Smith Aircraft in attempting to defraud the Shackets; and that Philko and McArdle joined Smith and Smith Aircraft in the illegal and fraudulent conversion of the Shackets' property. Except for the issue of conversion, which is a matter of law and follows from the matters already discussed in this opinion, there is no evidence in support of the allegations in Count II.[13] Certainly there is no showing of fraud or a knowing interference with the Shackets' rights by Philko or McArdle.

Defendants' memorandum in support of the McArdle-Philko cross-motion for summary judgment regarding Count II was not responded to by Shackets. Accordingly the Court finds there is no genuine issue of any material fact regarding the subject matter of Count II.

Conclusion

This Court finds that there is no genuine issue as to any material fact in this action, that plaintiffs are entitled to judgment as a matter of law with respect to Count I and that defendants Philko and McArdle are entitled to judgment as a matter of law with respect to Count II. Counsel are directed to submit a form of final judgment for entry by the Court on or before September 29, 1980.

/s/ Milton I. Shadur
United States District Judge

Date: September 22, 1980

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[13] At the Shacket-Smith Aircraft closing, Rittenhouse told Shacket that Smith had a partner named Philko. Sometime after both "sales," McArdle told Shacket there was money owed on the plane. Neither of those facts creates an issue of fact supporting the allegations of Count II.

APPENDIX D

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

MAURICE SHACKET and
SYLVIA SHACKET,
Plaintiffs,

v.

ROGER SMITH AIRCRAFT
SALES, INC., et al.,
Defendants.

PHILKO AVIATION, INC.,
Counter-Plaintiffs,

v.

MAURICE SHACKET, et al.,
Counter-Defendants.

SANDWICH STATE BANK,
Counter-Plaintiff,

v.

MAURICE SHACKET, et al.,
Counter-Defendants.

No. 78 C 4284

MEMORANDUM OPINION AND ORDER

Defendant Philko Aviation, Inc. ("Philko") has filed a "Motion pursuant to Rule 60(b) for modification of the Order of Court granting the plaintiffs' Motion for Summary Judgment."[1] For the reasons stated in this memorandum opinion and order, Philko's motion is granted to a limited extent but is denied in all principal respects.

Payment of Value by Shackets

There is no question that Shackets paid value for the aircraft. Philko's arguments to the contrary do not reach the level of surface plausibility needed to characterize them as even specious, for Philko ignores entirely Shacket's payment of *$126,000* in *cash* in addition to his delivery of possession of a trade-in plane worth another *$120,000* at wholesale. Indeed, even on the latter score what Philko seeks to rely on are statements by Shacket in December 18, 1979 answers to interrogatories in a Minnesota state court action.[2] There Shacket's claim

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[1] Philko's motion was filed 80 days after the Court's September 22, 1980 memorandum opinion and order (the "Opinion") granting plaintiffs' motion for summary judgment as to Count I of the Complaint. If Philko's motion were literally under Fed. R. Civ. P. ("Rule") 60(b), the Court would be disposed to hold that it had not been timely filed under Rule 59(e) and had not been "made within a reasonable time" under Rule 60(b) and was therefore not sustainable. But plaintiffs did not, as the September 22 Opinion directed, submit a definitive form of final judgment and order for entry by the Court. Because other claims were involved in the action, the Opinion did not constitute a *final* judgment (see Rule 54(b)), and Rule 60(b) thus appears to be inapplicable.

[2] Philko did not initially submit that interrogatory answer as one of the documents it relied on in opposition to Shackets' summary judgment motion or in support of Philko's own cross-motion. Even though the cross-motions had been fully briefed before the interrogatory answer was filed in the other litigation on June 20, 1980, Philko would presumably have had ample opportunity to deliver the document to this Court

(Footnote continued on following page)

that he still "owned" the old aircraft was stated as a conclusion in the context of "hold[ing] the title papers in my possession until the transaction with the new airplane would be completed and when he delivered to me the title on the new airplane, I would deliver to him the paperwork or title on the old airplane." Those *title papers* to the old aircraft were retained instead of a bank escrow by way of *security*, to protect himself pending completion of the purchase transaction. Philko again betrays its erroneous one-to-one identification of *title* transfers with *ownership*—ignoring, as it does on the principal claim in this lawsuit, the common commercial practice of using title retention for *security* purposes. But in all events the payment of *value* by Shackets cannot be disputed.

Shackets' Status as Good Faith Buyers

Nothing in Philko's motion derogates from the Court's discussion of the issue of Shackets' good faith (see Opinion 13-15). Philko persists in missing the whole point that whatever question existed as to *Smith's* right to the aircraft was a question vis-a-vis *Clark Aircraft*. And on that score the Court need do nothing more than repeat the statement at Opinion 15:

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[2] *continued*

and opposing counsel well before the Opinion was rendered September 22, 1980. Under the circumstances it is at best doubtful whether the material satisfies the "newly discovered evidence" standard of Rule 60(b)(2) or the "excusable neglect" test of Rule 60(b)(1). Nonetheless the Court has considered the interrogatory answer for purposes of this ruling. In that respect, the Court observes parenthetically that in speaking of that answer, Philko says that "as of June 20, 1980 Maurice Shacket averred under oath that he is still the owner of the old aircraft." In fact, Shacket's answer to interrogatories was signed and notarized in December, 1979, though filed in a Minnesota state court in 1980. Philko's carelessness with the facts and with its statement of the holdings in the Opinion discussed later is not such as to inspire confidence in Philko's arguments generally.

> As for Shacket's awareness of Smith Aircraft's financial problems, Shacket had no obligation to monitor Smith Aircraft's financial arrangements with Clark (a matter between those two parties), and Shacket's failure to do so does not bear on the issue of his good faith. Instead, Rittenhouse's response to Shacket at the closing that it was all right to proceed—after Rittenhouse had specifically asked to be present—conclusively rejects any lack of good faith, which the parties agree is the material fact on this issue (citing *Tumber v. Automation Design & Mfg. Co.*, 130 N.J. Super. 5. 324 A.2d 602 (1974)).

Philko also blurs the issue by misstating the Opinion's characterization of the agency question. It is fundamental law that agency cannot be created by the purported agent's self-use of that term. As the Court stated at Opinion 13, the mark of an agency relationship here would be that "if Smith Aircraft were acting as an agent and not as a principal for its own account, the purchase transaction with Clark, *including the price of the aircraft as negotiated by Smith*, would have had to be for the direct benefit of Shacket."[3] What Philko still does not want to understand is that if an *agent* makes a deal for his principal, the price that the agent commits for is the price the *principal* pays. That was plainly not so here, where Smith Aircraft was plainly dealing for its own account in the purchase from Clark Aircraft.

Non-Material Errors in the Opinion

In assembling its statement of facts from the materials submitted by the parties in support of their cross-motions for summary judgment, the Court apparently erred as to the date of the original Smith-McArdle contact regarding the aircraft. As Philko has pointed out, that appears to have occurred after rather than before the Shacket-Smith closing. Accordingly the

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[3] In referring to the Court's opinion in that respect, Philko deliberately omitted the underlined clause, which is the decisive indicium of agency lacking in this case.

first full paragraph at Opinion 5 should be revised to read:

> Before the events described in the prior section, McArdle had been pressuring Smith to repay the remaining balance of $60,000 on Philko's $80,000 loan made to Smith Aircraft in December 1977. On April 21, 1978, two days after the closing with Shacket, Smith came to McArdle and represented that he had contracted to purchase a plane (which was in fact the same plane that had been paid for by and delivered to Shacket) for resale to a third party, Krueger Aviation. Smith claimed to have tried to borrow $152,000 from Bank on the plane but to have been refused because that would have exceeded his line of credit with Bank.

At the top of Opinion 6, the reference to April 22, 1978 as two days after the Shacket transaction should be changed to *three* days.

Neither of those inadvertent errors is in any respect relevant to the substantive discussion in the Opinion. They have no bearing on the legal issues, as to which the relative timing of the two Smith transactions is wholly immaterial.

Philko's Status as a "Purchaser" or "Buyer"

Philko distorts both the Opinion and the record on this issue. It is plain that McArdle's understanding was that the funds from resale of the aircraft would *not* inure to Philko's benefit but to Smith Aircraft's. As Opinion 18 stated:

> Thus it is plain from his own testimony McArdle had no interest in the sale price to be paid by Krueger Aviation, except to make sure it was adequate to pay the bank loan and the $60,000 balance owed to Philko. That is the conclusive hallmark of a *credit* transaction not a *purchase.*

There is only one respect in which the Court finds it necessary to clarify its Opinion in the "purchaser" section. At various points in the discussion the Court used the terms "purchaser" and "buyer" interchangeably, not

as terms of art but in the common parlance in which they are synonyms. Under the UCC, however, the critical and more precise terminology—and the terminology the Court should have used throughout—relates to the parties' status or lack of status as *buyers* not *purchasers.*

As Opinion 19 stated, under UCC §1-202(9) "buying" specifically does not include a transfer as security. Accordingly, for the reasons stated in the Opinion Shacket *was* and Philko *was not* a "buyer"—and hence a "buyer in the ordinary course of business." Thus the case presents a conflict between a buyer in the ordinary course of business (Shacket) who failed to record a transaction, and the holder of a subsequently recorded security interest (Philko). All the Court's references at Opinion 19-20 to "bona fide purchaser" should be read as "buyer in the ordinary course of business"—and so read, all of the authorities therein cited support the Court's reasoning and conclusion in the Opinion. They confirm the superiority of the interest of a "buyer" to that of a secured party (see UCC §9-307).

As for Philko's other arguments, they offer nothing other than matters that were urged upon and rejected by the Court in the parties' original briefing. They require no discussion other than that already contained in the Opinion.

Conclusion

Except for the minor and non-dispositive respects in which this memorandum opinion and order has modified the Opinion, Philko's motion is denied. Counsel for plaintiffs are again directed to submit a form of final judgment for entry by the Court on or before January 27, 1981.

/s/ Milton I. Shadur
United States District Judge

Date: January 19, 1981

APPENDIX E

FORM APPROVED OMB NO. 04-R0016

UNITED STATES OF AMERICA
DEPARTMENT OF TRANSPORTATION
FEDERAL AVIATION ADMINISTRATION

DO NOT WRITE IN THIS BLOCK FOR FAA USE ONLY

0 0 0 0 0 0 6 4 2

AIRCRAFT BILL OF SALE

C I 7 2 5 4 6

FOR AND IN CONSIDERATION OF $ THE UNDERSIGNED OWNER(S) OF THE FULL LEGAL AND BENEFICIAL TITLE OF THE AIRCRAFT DESCRIBED AS FOLLOWS:

AIRCRAFT MAKE AND MODEL
Piper PA-31

MANUFACTURER'S SERIAL NUMBER
31-7812074

NATIONALITY & REGISTRATION MARKS
N78MS

DOES THIS 24th DAY OF April 1978 HEREBY SELL, GRANT, TRANSFER AND DELIVER ALL RIGHTS, TITLE, AND INTERESTS IN AND TO SUCH AIRCRAFT UNTO:

JUN 13 7 40 AM '78
FEDERAL AVIATION ADMINISTRATION
CONVEYANCE

PURCHASER

NAME AND ADDRESS
(IF INDIVIDUAL(S), GIVE LAST NAME, FIRST NAME, AND MIDDLE INITIAL)

Philko Aviation, Inc.
c/o Aurora Municipal Airport
Sugar Grove, Illinois 60554

AND TO EXECUTORS, ADMINISTRATORS, AND ASSIGNS TO HAVE AND TO HOLD SINGULARLY THE SAID AIRCRAFT FOREVER, AND WARRANTS THE TITLE THEREOF

IN TESTIMONY WHEREOF I HAVE SET my HAND AND SEAL THIS 24th DAY OF 4 1978

SELLER

NAME (S) OF SELLER (TYPED OR PRINTED)	SIGNATURE (S) (IN BLACK INK.) (IF EXECUTED FOR CO-OWNERSHIP, ALL MUST SIGN.)	TITLE (TYPED OR PRINTED)

#-2 - 3 - 1

ACKNOWLEDGMENT (NOT REQUIRED FOR PURPOSES OF FAA RECORDING - HOWEVER, MAY BE REQUIRED BY LEGAL LAW FOR VALIDITY OF THE INSTRUMENT.)

ORIGINAL - TO FAA

$5.00

FORM APPROVED
OMB NO. 04-R0293

UNITED STATES OF AMERICA
DEPARTMENT OF TRANSPORTATION — FEDERAL AVIATION ADMINISTRATION

AIRCRAFT BILL OF SALE

8 0 0 0 0 0 6 4 1

FEDERAL AVIATION ADMINISTRATION
JUN 12 / 00 AM '78

CONVEYANCE

C 172547

FOR AND IN CONSIDERATION OF $ 1.00 THE UNDERSIGNED OWNER(S) OF THE FULL LEGAL AND BENEFICIAL TITLE OF THE AIRCRAFT DESCRIBED AS FOLLOWS:

UNITED STATES REGISTRATION NUMBER: N 78MS

AIRCRAFT MANUFACTURER & MODEL: Piper PA-31

AIRCRAFT SERIAL No.: 31-7812074

DOES THIS 20th DAY OF April 19 78 HEREBY SELL, GRANT, TRANSFER AND DELIVER ALL RIGHTS, TITLE, AND INTEREST IN AND TO SUCH AIRCRAFT UNTO:

Do Not Write In This Block FOR FAA USE ONLY

PURCHASER

NAME AND ADDRESS
(IF INDIVIDUAL(S), GIVE LAST NAME, FIRST NAME, AND MIDDLE INITIAL.)

Roger Smith Aircraft Sales, Inc.
Aurora Municipal Airport
Sugar Grove, Ill 60554

DEALER CERTIFICATE NUMBER

AND TO their EXECUTORS, ADMINISTRATORS, AND ASSIGNS TO HAVE AND TO HOLD SINGULARLY THE SAID AIRCRAFT FOREVER, AND WARRANTS THE TITLE THEREOF.

IN TESTIMONY WHEREOF I HAVE SET our HAND AND SEAL THIS 20th DAY OF Apr 19 78

SELLER	NAME (S) OF SELLER (TYPED OR PRINTED)	SIGNATURE (S) (IN INK) (IF EXECUTED FOR CO-OWNERSHIP, ALL MUST SIGN.)	TITLE (TYPED OR PRINTED)
	Clark Aviation, Inc	Kenneth Kitchen	President

ACKNOWLEDGMENT (NOT REQUIRED FOR PURPOSES OF FAA RECORDING; HOWEVER, MAY BE REQUIRED BY LOCAL LAW FOR VALIDITY OF THIS INSTRUMENT.)

ORIGINAL: TO FAA

AC FORM 8050-2 (5-72) (8052-035-0002)

FORM APPROVED
OMB NO. 04-R0019

UNITED STATES OF AMERICA
DEPARTMENT OF TRANSPORTATION

AIRCRAFT BILL OF SALE

0 0 0 0 0 0 6 1 7 2 5 4 4

JUN 13 7 40 AM '78
CONVEYANCE
CLERK
DEPT. OF TRANSPORTATION

FOR AND IN CONSIDERATION OF $1.00&OVC&K, UNDERSIGNED OWNER(S) OF THE FULL LEGAL AND BENEFICIAL TITLE OF THE AIRCRAFT DESCRIBED AS FOLLOWS:

UNITED STATES REGISTRATION NUMBER N 78MS

AIRCRAFT MANUFACTURER & MODEL Piper PA-31-325

AIRCRAFT SERIAL No. 31-7812074

DOES THIS 18th DAY OF April 19 78 HEREBY SELL, GRANT, TRANSFER AND DELIVER ALL RIGHTS, TITLE, AND INTERESTS IN AND TO SUCH AIRCRAFT UNTO:

Do Not Write In This Block
FOR FAA USE ONLY

PURCHASER

NAME AND ADDRESS
(IF INDIVIDUAL(S), GIVE LAST NAME, FIRST NAME, AND MIDDLE INITIAL.)

CLARK AVIATION, INC.
Bloomington-Normal Airport
Bloomington, Illinois 61701

DEALER CERTIFICATE NUMBER

AND TO their EXECUTORS, ADMINISTRATORS, AND ASSIGNS TO HAVE AND TO HOLD SINGULARLY THE SAID AIRCRAFT FOREVER, AND WARRANTS THE TITLE THEREOF.

IN TESTIMONY WHEREOF WE HAVE SET OUR HAND AND SEAL THIS 18 DAY OF April 19 78

SELLER

NAME (S) OF SELLER (TYPED OR PRINTED)	SIGNATURE (S) (IN INK) (IF EXECUTED FOR CO-OWNERSHIP, ALL MUST SIGN.)	TITLE (TYPED OR PRINTED)
NORTH STATES AVIATION, INC.	Bill J. Tausend	Manager

ACKNOWLEDGMENT (NOT REQUIRED BY FAA FOR CITIZENS OF U.S., BUT MAY BE REQUIRED BY LOCAL LAW FOR VALIDITY OF THIS INSTRUMENT.)

ORIGINAL: TO FAA

FORM APPROVED
OMB NO. 04-R0025

UNITED STATES OF AMERICA
DEPARTMENT OF TRANSPORTATION

AIRCRAFT BILL OF SALE

0 0 0 0 0 2 1 6 1 7 2 5 4 3

FOR AND IN CONSIDERATION OF $1.00 &ovr; THE UNDERSIGNED OWNER(S) OF THE FULL LEGAL AND BENEFICIAL TITLE OF THE AIRCRAFT DESCRIBED AS FOLLOWS:

1 UNITED STATES REGISTRATION NUMBER N N78MS

AIRCRAFT MANUFACTURER & MODEL Piper PA-31

AIRCRAFT SERIAL No. 31-7812074

DOES THIS 18th DAY OF April 19 78 HEREBY SELL, GRANT, TRANSFER AND DELIVER ALL RIGHTS, TITLE, AND INTERESTS IN AND TO SUCH AIRCRAFT UNTO:

JUN 13 / 40 PM '78
FEDERAL AVIATION ADMINISTRATION
CONVEYANCE SECTION

Do Not Write In This Block
FOR FAA USE ONLY

PURCHASER

NAME AND ADDRESS
(IF INDIVIDUAL(S), GIVE LAST NAME, FIRST NAME, AND MIDDLE INITIAL.)

NORTH STATES AVIATION, INC.
4521 Patterson S.E.
Grand Rapids, MI 49508

DEALER CERTIFICATE NUMBER

AND TO their EXECUTORS, ADMINISTRATORS, AND ASSIGNS TO HAVE AND TO HOLD SINGULARLY THE SAID AIRCRAFT FOREVER, AND WARRANTS THE TITLE THEREOF.

IN TESTIMONY WHEREOF WE HAVE SET OUR HAND AND SEAL, THIS 18 DAY OF April 78

SELLER

NAME (S) OF SELLER (TYPED OR PRINTED)	SIGNATURE (S) (IN INK) (IF A CORPORATION, FOR CO-OWNERSHIP, ALL MUST SIGN.)	TITLE (TYPED OR PRINTED)
Piper Aircraft Corporation	[signature]	Manager of Sales

ACKNOWLEDGMENT (IF REQUIRED BY LOCAL LAW FOR RECORDING IN THE JURISDICTION.)

My Commission Expires March 14, 1980

ORIGINAL: TO FAA

AC FORM 8050-2 (1-72) (SUPERSEDES)

[signature]

APPENDIX F

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

U.S. Const. art. VI

Article VI

* * *

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

49 U.S.C. Sec. 1403 (1981)

§ 1403. Recordation of aircraft ownership

(a) Establishment of recording system. The Administrator [Secretary of Transportation] shall establish and maintain a system for the recording of each and all of the following:

(1) Any conveyance which affects the title to, or any interest in, any civil aircraft of the United States;

(2) Any lease, and any mortgage, equipment trust, contract of conditional sale, or other instrument executed for security purposes, which lease or other instrument affects the title to, or any interest in, any specifically identified aircraft engine or engines of seven hundred and fifty or more rated takeoff horsepower for each such engine or the equivalent of such horsepower, or any specifically identified aircraft propeller capable of absorbing seven hundred and fifty or more rated takeoff shaft horsepower, and also any assignment or amendment thereof or supplement thereto;

(3) Any lease, and any mortgage, equipment trust, contract of conditional sale, or other instrument executed for security purposes, which lease or other instrument affects the title to, or any interest in, any aircraft engines, propellers, or appliances maintained by or on behalf of an air carrier certificated under section 604(b) of this Act [49 USCS § 1424(b)] for installation or use in aircraft, aircraft engines, or propellers, or any spare parts maintained by or on behalf of such an air carrier, which instrument need only describe generally by types the engines, propellers, appliances, and spare parts covered thereby and designate the location or locations thereof; and also any assignment or amendment thereof or supplement thereto;

(b) Recording of releases, cancellations, discharges, or satisfactions. The Administrator [Secretary of Transportation] shall also record under the system provided for in subsection (a) of this section any release, cancellation, discharge, or satisfaction relating to any conveyance or other instrument recorded under said system.

(c) Validity of conveyances or other instruments, filing. No conveyance or instrument the recording of which is provided for by section 503(a) [subsec. (a) of this section] shall be valid in respect of such aircraft, aircraft engine or engines, propellers, appliances, or spare parts against any person other than the person by whom the conveyance or other instrument is made or given, his heir or devisee, or any person having actual notice thereof, until such conveyance or other instrument is filed for recordation in the office of the Administrator [Secretary of Transportation]: Provided, That previous recording of any conveyance or instrument with the Administrator of the Civil Aeronautics Administration under the provisions of the Civil Aeronautics Act of 1938 shall have the same force and effect as though recorded as provided herein; and conveyances, the recording of which is provided for by section 503(a)(1) [subsec. (a)(1) of this section] made on or before August 21, 1938, and instruments, the recording of which is provided for by sections 503(a)(2) and 503(a)(3) [subsecs. (a)(2) and (a)(3) of this

section] made on or before June 19, 1948, shall not be subject to the provisions of this subsection.

(d) Effect of recording. Each conveyance or other instrument recorded by means of or under the system provided for in subsection (a) or (b) of this section shall from the time of its filing for recordation be valid as to all persons without further or other recordation, except that an instrument recorded pursuant to section 503(a)(3) [subsec. (a)(3) of this section] shall be effective only with respect to those of such items which may from time to time be situated at the designated location or locations and only while so situated: Provided, That an instrument recorded under section 503(a)(2) [subsec. (a)(2) of this section] shall not be affected as to the engine or engines, or propeller or propellers, specifically identified therein, by any instrument theretofore or thereafter recorded pursuant to section 503(a)(3) [subsec. (a)(3) of this section].

(e) Form of conveyances or other instruments. Except as the Administrator [Secretary of Transportation] may by regulation prescribe, no conveyance or other instrument shall be recorded unless it shall have been acknowledged before a notary public or other officer authorized by the law of the United States, or of a State, territory, or possession thereof, or the District of Columbia, to take acknowledgment of deeds.

(f) Index of conveyances and other instruments. The Administrator [Secretary of Transportation] shall keep a record of the time and date of the filing of conveyances and other instruments with him and of the time and date of recordation thereof. He shall record conveyances and other instruments filed with him in the order of their reception, in files to be kept for that purpose, and indexed according to—

(1) the identifying description of the aircraft, aircraft engine, or propeller, or in the case of an instrument referred to in section 503(a)(3) [subsec. (a)(3) of this section], the location or locations specified therein; and

(2) the names of the parties to the conveyance or other instrument.

(g) Regulations. The Administrator [Secretary of Transportation] is authorized to provide by regulation for the endorsement upon certificates of registration, or aircraft certificates, of information with respect to the ownership of the aircraft for which each certificate is issued, the recording of discharges and satisfactions of recorded instruments, and other transactions affecting title to or interest in aircraft, aircraft engines, propellers, appliances, or parts, and for such other records, proceedings, and details as may be necessary to facilitate the determination of the rights of parties dealing with Civil aircraft of the United States, aircraft engines, propellers, appliances, or parts.

(h) Previously unrecorded ownership of aircraft. The person applying for the issuance or renewal of an airworthiness certificate for an aircraft with respect to which there has been no recordation of ownership as provided in this section shall present with his application such information with respect to the ownership of the aircraft as the Administrator [Secretary of Transportation] shall deem necessary to show the persons who are holders of property interests in such aircraft and the nature and extent of such interests.

49 U.S.C. Sec. 1406 (1981)

§ 1406. Law governing validity of certain instruments

The validity of any instrument the recording of which is provided for by section 503 of this Act [49 USCS § 1403] shall be governed by the laws of the State, District of Columbia, or territory or possession of the United States in which such instrument is delivered, irrespective of the location or the place of delivery of the property which is the subject of such instrument. Where the place of intended delivery of such instrument is specified therein, it shall constitute presumptive evidence that such instrument was delivered at the place so specified.

Ill. Rev. Stat. Ch. 26, Sec. 2-403 (1978)

§ 2-403. Power to Transfer; Good Faith Purchase of Goods; "Entrusting"

(1) A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though

(a) the transferor was deceived as to the identity of the purchaser, or

(b) the delivery was in exchange for a check which is later dishonored, or

(c) it was agreed that the transaction was to be a "cash sale", or

(d) the delivery was procured through fraud punishable as larcenous under the criminal law.

(2) Any entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business.

(3) "Entrusting" includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor's disposition of the goods have been such as to be larcenous under the criminal law.

(4) The rights of other purchasers of goods and of lien creditors are governed by the Articles on Secured Transactions (Article 9), Bulk Transfers (Article 6) and Documents of Title (Article 7). 1961, July 31, Laws 1961, p. 2101, § 2-403.